CANADIAN BANKING LEGISLATION

The new Canadian banking bill was introduced in the Dominion Parliament, in session at Ottawa, by Hon. W. T. White, minister of finance, and given its first reading on December 17, 1912. It has already been the subject of careful consideration by the Minister, the leading bankers, and the Canadian press, and will doubtless become law without important alteration. The decennial revision would regularly have been made in 1910; but, owing to the wrecking of the Farmers' Bank and the consequent state of public opinion, it was wisely deferred for two years by acts of May 19, 1911, and May 4, 1912. The delay has proved of advantage. It is generally admitted that an admirable piece of legislation has been produced, without any serious hindrance from the seekers for political capital. The charters of the banks will be extended by the legislation now pending until July 1, 1923.

The new act embodies a number of very important innovations. They may be summarized as follows:

1. More stringent provisions against malpractices, including additional safeguards against fraudulent organization, the requirement of more detailed returns, and a compulsory annual shareholders' audit.

2. An extension of the banks' authority to grant credit, by the authorization of loans upon farm stock and grain in storage as legal security.

3. An enlargement of the banks' power of issue by the authorization of additional notes, based dollar for dollar upon the deposit of gold or Dominion notes in the "Central Gold Reserves," administered by a board of trustees.

Additional safeguards have been thrown about the organization of banks, calculated to protect subscribers during the interval between the incorporation of the bank and the authorization, by the Treasury Board, of the commencement of business and of note-issue. Excepting ordinary disbursements of a necessary character,

no expenditure may legally be made by the provisional directors or the Board of Directors, unless authorized by resolution of the subscribers, until a certificate has been obtained from the Treasury Board. The certificate may not issue until the board is satisfied that all the expenses of incorporation and organization in connection with commissions and other items of a similar nature are reasonable. A further important protection is the requirement that the double-liability clause must be printed on each page of the stock books and on every document constituting or authorizing a subscription, so as to be readily seen.

Within the past year considerable anxiety has been evidenced in some circles in regard to bank mergers and the consequent concentration and centralization of banking power. Some feeling was aroused in opposition to the amalgamation of the Royal and Traders' banks, a merger which followed closely upon two other absorptions induced by rivalry of the two largest Canadian banks. Rumor has repeatedly merged several other institutions. In future, the consent of the minister of finance must be obtained before an agreement to amalgamate may legally be entered into by the directorates of the institutions involved.

The annual financial statement, required under the present bank act to be presented by the directors to the shareholders of the respective banks, has remained since 1854 without material change, as part of Canadian banking legislation. Both the statement to the shareholders and the monthly return to the Department of Finance have been elaborated in the revised act, and particulars have been called for beyond the requirements of existing regulations. The intention is to present to the shareholders and the government, respectively, a particularized, detailed statement of the assets and liabilities of the banks, properly grouped and showing as fairly as may be the financial position of each of the chartered banks.

Sentiment in favor of the establishment of adequate checks upon the general management of Canadian banks has been steadily gaining strength since the failure of the Ontario Bank in 1906. Branches are subject to rigorous examination by inspectors from the head office, but there is no one to watch the general manager

or the ledger at headquarters. Theoretically, this duty devolves upon the directors, but evidence is not wanting that boards of directors do not always direct and that they may easily be kept in the dark as to the actual character of their bank's transactions. Unquestionably, there is danger of fabricated balance sheets, incorrect reports, and other banking malpractices. A check on the general management at the head office is provided in the new bill and is expected to operate effectively against the recurrence of discreditable failures such as those of the Ontario, Sovereign, and Farmers' banks within the recent banking history of Canada.

Numerous suggestions have been made, trenchantly attacked, and as stoutly defended. Hon. Mr. White is opposed to making the government undertake what can be done with at least equal efficiency by mutual associations or other agencies. In the view that the Dominion government should not assume a regular inspection of the banks, the Minister was supported by the press and the public generally, inasmuch as it was clearly recognized that such an inspection could not be thorough, and that it would not offer a real guaranty of solvency, or provide for certain detection of wrongdoing. On the other hand, the bankers themselves were unable to agree upon the matter of inspection by the Canadian Bankers' Association. Popular sympathy was with the smaller institutions to which the suggestion of coercion contained in the proposal was distasteful. Consequently, though offering many theoretical advantages, such a system was manifestly impracticable at the present time, A course was adopted midway between government inspection and internal examination conducted by the Canadian Bankers' Association.

The new provisions follow the English legislation in regard to the audit of the large joint stock companies. At each annual general meeting the shareholders are required to appoint an auditor or auditors, who shall certify "whether, in their opinion, the statement referred to in the report is properly drawn up, so as to exhibit a true and correct view of the state of the bank's affairs, according to the best of their information and the explanations given to them, and as shown by the books of the bank." Such a report is to be attached to the annual statement presented to the shareholders.

Should the minister deem a more searching inquiry advisable, he may require an auditor to make a special examination and report to him as head of the Finance Department. For such special service the auditor is to be remunerated out of the Federal Consolidated Revenue Fund. Although somewhat experimental, the system of external audit thus provided for would appear to have practically all the advantages of government inspection, without the obvious disadvantages entailed in the latter. The banking bill of the minister of finance in the last Liberal cabinet, Hon. W. S. Fielding, made the shareholders' audit optional. Several banks have already adopted the system of their own volition, but the practice is not yet general. By the pending legislation, in addition to the penalties imposed by existing legislation for wilful misrepresentation, deception, or falsification, directors, officers, and auditors are made liable to indictment and punishment for negligently preparing or making false and deceptive statements.

For some time there has been a growing agitation among the grain-growers of western Canada for increased banking accommodation, and this despite the fact that, as recently pointed out, loans west of the Great Lakes, by the chartered banks, are doubl the amount of capital supplied by that part of the Dominion as deposits. In both Alberta and Saskatchewan, the provincial legislatures have gone so far as to consider the feasibility of state loans to agriculturists. Lack of adequate transportation facilities to handle the large grain crop and the practical absence as yet of mixed farming in western Canada would seem to call for some relaxation of the present stringent regulations concerning the security upon which the banker may lend, and to justify the authorization in the present bill of loans upon threshed grain in storage as well as in transit. A rancher's cattle are also to be made legal security for banking accommodation. Such credit may, it is true, partake rather of the nature of mortgage than of commercial loans. But in view of a national problem involved, and the need of finding a remedy for a somewhat acute economic situation, the result largely of geographical and topographical conditions, the action of the Minister of Finance in proposing the legalization of such security to the

chartered banks is not inappropriate. It has the approval of members on both sides of the House, of the most conservative Canadian bankers, of the press, and of the general public. The two empowering clauses (§ 88, 2, 3) read: "The bank may lend money to a farmer upon the security of his threshed grain (of any kind) grown upon the farm." "The bank may lend money to a rancher upon the security of his cattle." The same privileges will, of course, be enjoyed by the agriculturist of eastern Canada, as by his fellow, whether farmer or stock-breeder, in the western provinces. The banks may also lend money to a receiver or liquidator under a general winding-up act.

The remaining important innovation of the new bill was doubtless suggested by the recommendations of Senator Aldrich and the National Monetary Commission for the establishment of a National Revenue Association in the United States, and by European banking legislation and practices. The immediate proposal came from the Canadian bankers themselves. Section 61 empowers any chartered bank to extend its note circulation beyond the maximum now authorized, upon depositing dollar for dollar, gold or Dominion notes, in the "Central Gold Reserves." The provision is well calculated to serve three distinct and important ends. Perhaps the most obvious is the accumulation of a large visible supply of gold in Canada. This cannot fail to add another factor of stability to the Canadian banking system. Banking can be conducted most economically, to the mutual benefit of the banks and their customers, only when public confidence is present in a high degree. Confidence in the ability of banks to pay is best inspired and maintained by a large visible means of payment.

Second, the provision promises a solution of the currency problem. The banks will be enabled to emit a bank note circulation which will be perfectly elastic, both as regards expansion and contraction. No legal maximum is imposed, and notes may be issued to any amount, provided the excess of the circulation above that authorized under other sections of the bank act is covered, in full, by gold or Dominion notes, which are practically gold certificates. Ultimately, doubtless, the Canadian bank note circulation will become

like that of the Bank of England, with a fixed amount issued upon general assets and a large balance fully covered by gold. The volume which may be issued upon securities will, however, not be rigid, but will vary as the combined paid-up capital of the issuing institutions is increased. Canada will thus be provided with a note circulation absolutely responsive to the needs of trade.

Third, a means of profitable employment will be afforded for the reserves now carried by those banking institutions, which, in accordance with conservative policy, maintain large amounts of cash on hand. In time, too, the provision may operate to check the periodic flow of gold from the Canadian banks to New York.

It is interesting to note that the new bill, described by some Opposition newspapers as a "mild expedient," is a measure of far-reaching importance and significance. It paves the way for the gradual evolution of the "Central Gold Reserves" in Canada and their management as an institution which, should such action be deemed advisable, might at some future date be vested with similar powers to those proposed for the National Reserve Association of the United States. The ease with which the Canadian banking legislation may be amended and adapted to new needs of a growing nation is a tribute to the efficiency of the system and another evidence of the truth of the statement that it is in constant process of evolution.

A greater measure of co-operation than at present exists must be expected among the banking institutions as in other lines of business. There are indications that organic combination among Canadian banks has about reached an end and that co-operation will be the keynote of future development. The Canadian Bankers' Association represents banking co-operation. It already exerts a wide and, on the whole, a desirable influence; and it may well be that, by the next revision of the bank act, conditions may be ripe for a further extension of its powers. In the present bill, the association is intrusted with the appointment of three custodians or trustees of "Central Gold Reserves," subject to the approval of the finance minister, who appoints the fourth. The association will bear all the expenses involved, including the remuneration of all four trustees. The reserve will be inspected at least semi-

annually, and should a depositing institution become insolvent, the amount held to its credit will be applied specifically in redemption of its notes outstanding.

No valid objection has yet openly been urged against Hon. Mr. White's proposal. In addition to a certain amount of perfunctory criticism from the Opposition benches, it is, to be sure, argued in some quarters that the bill does not go as far as it should. Fear, too, is expressed that the shareholders' audit will not provide as much protection for depositors and the general public as could be desired. The power and influence of the Canadian banks is also viewed by some with a feeling of trepidation and numerous suggestions are offered by which such power might be curtailed. Government issues of "printed promises," as a substitute for bank notes, have advocates in Parliament and outside. But such discussion is inevitable at the decennial revision of the Act. The bill is a government measure and no serious tampering is expected, nor will it be permitted. It has the hearty and unanimous indorsement of the bankers themselves, and seems likely to add to the efficiency of the Canadian banking system as an instrument of national economic development.

S. Roy Weaver

Toronto, Canada